

Message Text

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ACTION NEA-10

INFO OCT-01 ISO-00 EB-07 /018 W
-----030826Z 105589 /12

R 030625Z MAY 77
FM AMEMBASSY KUWAIT
TO SECSTATE WASHDC 7904
USDOC WASHDC
INFO AMEMBASSY ABU DHABI
USINT BAGHDAD
AMCONSUL DHAHRAN
AMEMBASSY DOHA
AMEMBASSY JIDDA
AMEMBASSY MANAMA
AMEMBASSY MUSCAT
AMEMBASSY TEHRAN

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USDOC FOR CAGNE

E.O. 11652: N/A
TAGS: ENRG, EIND
SUBJECT: EARLY WARNING- MAJOR TRADE OPPORTUNITY: POSSIBLE \$1 BILLION
KUWAIT REFINERY EXPANSION

1. SUMMARY: COMPUTER MODEL BASED STUDY OF KUWAIT'S ENERGY
AND PETROEUM PRODUCT NEEDS, FACTORING ON ENVIRONMENTAL CON-
SIDERATIONS, IS SCHEDULED FOR COMPLETION IN JULY. THIS AND OIL
MINISTER'S INTEREST IN EXPANDING REFINERY CAPACITY MAY HELP IN
RESOVING LONG-STANDING QUESTION OF WHETHER TO BUILD \$1 BILLION
EXPORT REFINERY, AND IF SO, WHICH OF TWO COMPETING NATIONALIZED
OIL COMPANIES WILL BUILD IT. IF APPROVED, REFINERY WOULD BE MAJOR TRA
DE
OPPORTUNITY FOR US FIRMS. END SUMMARY.

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2. FOR SOME TIME, TWO NATIONALIZED COMPANIES WITH THE TWO LARGEST
REFINERIES IN KUWAIT, THE KUWAIT NATIONAL PETROLEUM CO. (KNPC)
AND THE KUWAIT OIL COMPANY (KOC), HAVE BEEN VYING TO WIN
THE RIGHT TO BUILD NEW REFINERY CAPACITY, AT A LIKELY COST OF
\$500 MILLION TO OVER \$1 BILLION. ANY REFINERY CAPACITY EXPANSION
WILL DEPEND ON THE RESULT OF A BROAD GAUGE STUDY OF ENERGY NEEDS
AND USAGE IN KUWAIT, BEING DONE BY A TECHNICAL COMMITTEE,

UNDER THE SUPERVISION OF THE PETROLEUM PROJECTS PRIORITIES COMMITTEE, MADE UP OF REPS FROM MINISTRIES OF OIL, PLANNING, AND ELECTRICITY AND WATER, AS WELL REPS FROM THREE GOK-OWNED OIL COMPANIES, KNPC, KUWAIT OIL COMPANY (KOC) AND PETRO-CHEMICAL INDUSTRIES COMPANY (PIC).

3. BACKGROUND OF STUDY IS PROJECTED SHORTAGE OF NATURAL GAS, RESULTING FROM THE COMPLETION BY LATE 1978 9*)8173*83\$ 03549)37. GAS (LPG) PROJECT. PROJECT WOULD GATHER ALL OF KUWAIT'S GAS RESERVES, SOME OF WHICH ARE NOW FLARED, BUT WOULD PROCESS THEM INTO BUTANE, PROPANE AND ETHANE GAS FOR EXPORT AND FOR DOMESTIC INDUSTRIAL PURPOSES. THIS WOULD LEAVE KUWAIT SHORT OF GAS FOR ELECTRIC POWER PRODUCTION (AND WATER DISTILLATION) AT A TIME WHEN ELECTRIC POWER DEMAND IS RISING.

4. COMMITTEE HAS COMPLETED FIRST PART OF ITS TASK, TO DETERMINE THE ACTUAL MAGNITUDE OF THE PROSPECTIVE GAS SHORTAGE. (KOC SOURCES INDICATE THIS TO BE 600 MILLION CUBIC FEET P/D BY 1978, ASSUMING A 2 MILLION B/D PRODUCTION LEVEL.) STUDY, ON WHICH COMMITTEE NOW IS WORKING, WILL DETERMINE THE COSTS INVOLVED IN PRODUCING ENERGY FROM VARIOUS ALTERNATIVES--NATURAL GAS, GAS OIL, FUEL

OIL, CRUDE--AS WELL AS THE EFFECTS OF SUCH ALTERNATIVES ON THE ENVIRON-

MENT. KNPC HAS BEEN GIVEN PRIMARY RESPONSIBILITY FOR THIS PHASE, FOR WHICH IT IS MAKING USE OF COMPUTER MODELS. STUDY IS PROCEEDING WELL, AND SHOULD BE COMPLETED BY JULY 1977.

5. STUDY RESULTS WIL INFLUENCE COURSE OF GOK POLICY NOT ONLY IN LIMITED OFFICIAL USE

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REFINERY FIELD, BUT IN SUCH AREAS AS PETROCHMEICAL INDUSTRIES AND POLLUTION CONTROL. STATEMENT BY OIL MINISTER KAZIMI MAY 1, PRIOR TO LEAVING FOR OAPEC CONFERENCE, THAT KUWAIT IS KEEN TO EXPAND REFINERY CAPACITY IN ORDER TO TURN ITS HIGH SULFUR CRUDE INTO MORE MARKETABLE PRODUCTS, INDICATES THAT GOK MAY BE GIVING CLOSER CONSIDERATION TO QUESTION THAN IT HAS IN PAST.

6. KOC OR KNPC. RESULTS OF ENERGY STUDY ARE CRUCIAL TO SETTling QUESTION OF THE TYPE OF REFINERY EXPANSION TO BE BUILT IN KUWAIT. ISSUE HAS PITTED KOC AGAINST KNPC. PERHAPS REFLECTING THE EXPERIENCE OF ITS FORMER PARTNER, GULF, WHICH EMPHASIZED PRODUCTION OF FUEL OIL FOR EXPORT JAPAN MARKET, KOC HAS PROPOSED A MAJOR \$500 MILLION EXPANSION OF ITS OVER TWENTY YEAR OLD, 130,000 B/D "TOPPING" REFINERY. EXPANSION WOULD ADD DESULPHURIZING UNITS TO ENABLE REFINERY TO PRODUCE LOW SULPHUR CRUDE OIL FOR USE BOTH

IN OVERSEAS (PRIMARILY JAPANESE) MARKETS AND LOCAL ELECTRIC POWER PLANTS (WHICH WOULD BE, OR ARE ALREADY, CONVERTED TO BURN FUEL OIL). ADVANTAGES OF THIS APPROACH ARE LESSEned DEPENDENCE ON GAS PRO-

DUCTION, LOCAL UTILIZATION OF FUEL OIL WHICH DOES NOT HAVE A STRONG
INTERNATIONAL MARKET, AND REDUCTION IN ENVIRONMENTAL POLLUTION.

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INFO OCT-01 ISO-00 EB-07 /018 W
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FM AMEMBASSY KUWAIT
TO SECSTATE WASHDC 7905
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KNPC, ON THE OTHER HAND, ARMED WITH STUDIES BY BECHTEL, HAS PRO-
POSED A NEW 250,000 B/D REFINERY (COST: AT LEAST \$1 BILLION) BASICALL
Y
SIMILAR TO ITS OWN 195,000 B/D SHUAIBA FACILITY, WHICH WOULD PRODUCE
HIGHER PRICED MOTOR FUELS FOR THE INTERNATIONAL MARKET. KOC'S PLANS
ARE NOT IN KUWAIT'S INTEREST, KNPC SOURCE CLAIMED, BECAUSE
(1) THEY LOCK PRODUCTION INTO ONE PRODUCT, FUEL OIL, WHICH LIMITS
FOREIGN MARKETS, (2) LOW SULFUR FUEL OIL, REFINED TO MEET POLLUTION
STANDARDS OF JAPAN, IS A LUXURY POWER SOURCE FOR KUWAIT, WHICH DOES
NOT HAVE THE SAME POLLUTION PROBLEMS AS JAPAN. ONE KNPC SOURCE
PREDICTED THAT ENERGY STUDY RESULTS WOULD PROVE FAVORABLE TO KNPC
ALTERNATIVE, THOUGH HE DID ACKNOWLEDGE THAT PRODUCTION OF LOW SULPHUR
FUEL OIL FOR LOCAL MARKET WOULD RECEIVE SOME CONSIDERATION. HE PRE-
DICTED RESULTS WOULD BE "20PCT KOC, 80PCT KNPC" AND THAT SOME
DESULFURIZATION WILL BE INCLUDED. SHOULD KOC PROPOSAL BE SLECTED,
KNPC IS LEKELY TO PROPOSE A 100,000 B/D INCREASE IN ITS OWN
REFINERY CAPACITY.

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7. COMMENT: ECONOMIC, TECHNICAL, AND ENVIRONMENTAL, CONSIDERATIONS WILL UNDOUBTEDLY PLAY INFLUENTIAL ROLES IN THE ULTIMATE DECISION ON REFINERY EXPANSION AND GOK, VIA ITS ENERGY STUDY, IS ATTEMPTING TO ACQUIRE THE DATA BASE NECESSARY FOR EVALUATION OF THESE CONSIDERATIONS. HOWEVER, THE EFFECT OF BUREAUCRATIC RIVALRIES SHOULD NOT BE OVERLOOKED. THERE ARE CONTINUED DIFFERENCES IN OUTLOOK AMONG THE VARIOUS COMPONENTS OF KUWAIT'S OIL INDUSTRY, THEORETICALLY UNITED SINCE NATIONALIZATION. REFINERY EXPANSION QUESTION IS AN EXAMPLE: EACH COMPANY WANTS EXPANSION TO TAKE FORM OF THEIR CURRENT FACILITIES. WHILE UNABLE TO EVALUATE COMPLETELY VALIDITY OF KOC'S AND KNPC'S ARGUMENTS, WE SUGGEST THAT (1) KOC MAY BE OVERLY PESSIMISTIC ABOUT GAS AVAILABILITY AND NEED FOR FUEL OIL AS A RESULT OF OVER-ESTIMATING ITS OWN REINJECTION NEEDS AND IN UNDERESTIMATING AVAILABILITY OF KHAFJI (NEUTRAL ZONE) GAS AND OF FUTURE NON-ASSOCIATED GAS. (2) KNPC MAY BE EXAGGERATING ITS ABILITY TO MARKET OIL PRODUCTS INTERNATIONALLY, PARTICULARLY WHEN FACED WITH POSSIBLE GLUT IN REFINING CAPACITY FROM EUROPEAN AND NEWLY-BUILT MIDDLE EAST REFINERIES. HOWEVER, ADOPTION OF KOC PROPOSAL WOULD BE MUCH WELCOMED BY GULF, BECAUSE IT WOULD PROVIDE LATTER WITH SUPPLY OF LOW SULPHUR CRUDE WHICH WILL BE MUCH EASIER TO MARKET THAN PRESENT UNTREATED KUWAITI CRUDE. DECONTROL UPON RECEIPT. MAESTRONE

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